SUPREME COURT, U. S.

FILED

OCT 24 1975

IN THE

Supreme Court of the United States

OCTOBER TERM, 1975

75-625 4

Nos. ____ and ____

CAREY J. PERRY and MARIETTA M. PERRY, *Petitioners,*

v.

UNITED STATES OF AMERICA, *Respondent*

J. DOYLE MEDDERS and CONSTANCE P. MEDDERS, *Petitioners*

v.

UNITED STATES OF AMERICA, *Respondent*

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE FOURTH CIRCUIT

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UNITED STATES OF AMERICA, *Respondent*

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE FOURTH CIRCUIT

Petitioners pray that a Writ of Certiorari issue to review judgments of the United States Court of Appeals for the Fourth Circuit entered in these proceedings on July 29, 1975.

OPINION BELOW

The opinion of the United States Court of Appeals for the Fourth Circuit is reported at ____ F. 2d____, 36 AFTR 2d 75-5500 (the opinion is set out in full in the Appendix, 12a). The opinion of the United States District Court for the Eastern District of North Carolina is reported at 376 F. Supp. 15, 33 AFTR 2d 74-725 (E.D.N.C. 1974) (the opinion is set out in full in the Appendix 1a.)

JURISDICTION

The judgment of the United States Court of Appeals was entered July 29, 1975. Rehearing was not sought. This petition for certiorari was filed within 90 days of that date. The jurisdiction of this Court is invoked under 28 U.S.C. § 1254(1).

QUESTIONS PRESENTED

I. Where property has been donated to a trust and subsequently leased back to the donor by the trustee, is it necessary that a business purpose exist for the gift of the property to the donor as well as for the leaseback of the trust property to the donor in order for the rentals paid by the donor for the use of the trust property to be deductible by him under Section 162(a)(3) [26 U.S.C. § 162(a)(3)]?

II. Where property has been donated to a trust which has an independent trustee and said independent trustee subsequently leases said property back to the donor, is the donor's need for the use of the property in connection with the operation of his business a sufficient business purpose to render the rentals paid by the donor for the use of the trust property deductible by him under Section 162 (a)(3) [26 U.S.C. § 162(a)(3)]?

III. Whether the finding of a United States District Court that the trustee in a gift and leaseback transaction was independent is a finding of fact which must be respected, under Rule 52(a) of the Federal Rules of Civil Procedure [Fed. R. Civ. P. 52(a), 28 U.S.C.], by a Circuit Court of Appeals unless such finding was "clearly erroneous?"

STATUTES AND FEDERAL RULES INVOLVED

The statutory provision involved is Section 162(a)(3), of the Internal Revenue Code of 1954 [26 U.S.C. § 162(a)(3)], and is as follows:

> *"Sec. 162. Trade or Business Expenses.*
>
> "(a) *In General.*—There shall be allowed as a deduction all the ordinary and necessary expenses paid or incurred during the taxable year in carrying on any trade or business, including —
>
> . . . .
>
> "(3) rentals or other payments required to be made as a condition to the continued use or possession, for purposes of the trade or business, of property to which the taxpayer has not taken or is not taking title or in which he has no equity."

The Federal Rule involved is Rule 52(a), Fed. R. Civ. P., 28 U.S.C. which provides:

> "Rule 52. Findings by the Court.
>
> (a) Effect. In all actions tried upon the facts without a jury or with an advisory jury, the court shall find the facts specially and state separately its conclusions of law thereon, and judgment shall be entered pursuant to Rule 58; and in granting or refusing interlocutory injunctions the court shall similarly set forth the findings of fact and conclusions of law which constitute the grounds of its action. Requests for findings are not necessary for purposes of review. Findings of fact shall not be set aside unless clearly erroneous, and due regard shall be given to the opportunity of the trial court to judge of the credibility of the witnesses. The findings of a master, to the extent that the court adopts them, shall be considered as the findings of the court. If an opinion or memorandum of decision is filed, it will be sufficient if the findings of fact and conclusions of

law appear therein. Findings of fact and conclusions of law are unnecessary on decisions of motions under Rules 12 or 56 or any other motion except as provided in Rule 41(b)."

STATEMENT OF THE CASE

Carey J. Perry (hereinafter referred to as "Perry") and his wife, Marietta M. Perry, and J. Doyle Medders (hereinafter referred to as "Medders") and his wife, Constance D. Medders, are individuals residing in Louisburg, North Carolina. (R. 29).* Both the Perrys and the Medders timely filed joint federal income tax returns for the calendar year 1969 with the District Director of Internal Revenue for the District of North Carolina, using the cash basis method of accounting. (R. 29, 30).

Both Perry and Medders are licensed physicians. For a number of years, including 1969 and several years prior thereto, they have practiced as partners in Louisburg, North Carolina, in a medical partnership known as the Perry-Medders Clinic (hereinafter referred to as the "Partnership"). (R. 32).

Perry and Medders purchased a lot in Louisburg, North Carolina, as tenants in common and constructed a building thereon at a cost of $36,800.65 for use in conjunction with their medical practice (hereinafter referred to as the "Property"). (R. 32). Neither Mrs. Perry nor Mrs. Medders owned any interest in the Property. (R. 32). The Partnership first occupied the Property in July, 1963; and for the years of such occupancy, through 1968, it deducted a total of $9,295.87 as depreciation expenses on said building. (R. 32).

On December 16, 1968, Medders and Mrs. Medders, as grantors, and the Citizens Bank and Trust Company of

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* Such references are to pages of the "Appendix" filed with the Fourth Circuit.

Henderson, North Carolina (hereinafter referred to as the "Bank"), as trustee, entered into a trust agreement, the beneficiaries of which were the Medders' two children. (R. 33). The term of the trust created thereby was 14 years. (R. 17). On the same day Medders transferred to the trustee his undivided one-half interest in the Property. (R. 33). On the following day, December 17, 1968, the trustee, as lessor, and Medders, as lessee, entered into an agreement whereby the interest in the property previously conveyed to the trustee by Medders was leased back to Medders for a term of 14 years beginning December 17, 1968, at a rental rate of $200.00 per month. (R. 33-34).

On December 26, 1968, Perry and Mrs. Perry, as grantors, and the Bank as trustee, entered into a trust agreement, the beneficiaries of which were the Perrys' four children. (R. 33). The term of the trust created thereby was 10 years and 1 day. (R. 11). On the same day Perry transferred to the trustee his undivided one-half interest in the Property. (R. 33). On the following day, December 27, 1968, the trustee, as lessor, and Perry, as lessee, entered into an agreement whereby the interest in the Property previously conveyed to the trustee by Perry was leased back to Perry for a term of 10 years, beginning December 27, 1968, at a rental rate of $200.00 per month. (R. 33).

Except for the names of the grantors, beneficiaries, and length of term, the provisions of each of the two trust instruments are substantially identical: the grantor conveyed an undivided one-half interest in the Property (R. 9, 15); the trustee is the Bank (R. 9, 15); the trustee is authorized to hold, manage, and control and to collect and disburse the net income from the trust to or for the benefit of the respective grantors' children (R. 9, 15); upon the expiration of the specified term or upon the death of all of its grantors' children, whichever shall first occur, the trust shall terminate and its principal shall be distributed to its grantors if living, otherwise to its grantors' estates (R. 11, 17); the trustee is granted the "continuing absolute, discretionary power to deal

with any property, real or personal, held in any trust, as fully as [the grantors] might in the handling of [their] own affairs," with such powers to be exercised "independently and without prior or subsequent approval of any court or judicial authority" (R. 11, 17); and the trustee is granted all the powers set forth in North Carolina General Statute, § 32-27 (R. 11, 17). In addition, each trust agreement is irrevocable and unamendable and provides that its grantors shall have no right, title, or interest in any income accruing to the trust during its term and that its grantors shall have no incident of ownership in the assets making up the trust principal except the right to receive them upon termination of the trust. (R. 11, 17).

Except for the names of the lessees and the length of the respective terms, the provisions of each of the two lease agreements are substantially identical: a leasehold interest in an undivided one-half interest in the Property is conveyed at a rental of $200 per month (R. 21, 25); taxes and exterior repairs are to be paid by the lessor, and utilities and interior repairs are to be paid by the lessee (R. 22, 26); in the event of damage or destruction to the extent that the building cannot be repaired within 30 days, either party may terminate the lease upon written notice to the other party (R. 22, 26); and the lessor may terminate the lease and repossess the Property if the lessee defaults in any obligation under the lease and remains in default for 15 days after written notice calling his attention thereto (R. 22, 26).

During 1969 the Partnership paid a total of $4,800.00 to the Trustee as rent for the Property and claimed a rental deduction of $4,800.00 on its 1969 federal income tax return. (R. 34). The trustee-lessor reported the $4,800.00 received from the Partnership in 1969 as income for the respective trusts and claimed depreciation on said building. (R. 34).

Upon audit of the 1969 federal income tax returns of Perry and Medders, deficiencies in income tax were assessed against each of them, and each of them paid the amounts assessed and thereafter timely filed a claim for refund for

1969. (R. 30, 31). The refunds sought resulted from the determination by the Commissioner of Internal Revenue that the Partnership was not entitled to deduct $4,800.00 in rental payments made for the use of the Property during 1969. (R. 30, 31). Said claims for refund were disallowed, statutory notices of disallowance of their respective claims for refund were properly sent to Perry and Medders, and the present actions were timely instituted. The jurisdiction of the District Court was invoked under 28 U.S.C. § 1346 (a)(1).

After considering the stipulated facts, the trust agreements, the lease agreements, and legal authorities, the District Court concluded that Perry and Medders were entitled to the refunds sued for in these actions and that their consolidated motion for summary judgment should be allowed. Judgments were thereafter entered in favor of Perry and Medders, and the Respondent appealed to the United States Court of Appeals for the Fourth Circuit. (R. 49, 50). The Court of Appeals reversed the District Court and ordered judgment to be entered for the Respondent. (Appendix 19a).

REASONS WHY THE WRIT SHOULD BE GRANTED

I. THE DECISION OF THE COURT BELOW IS IN CONFLICT WITH THE DECISIONS OF OTHER COURTS OF APPEAL IN DETERMINING THE DEDUCTIBILITY OF RENTALS PAID IN GIFT AND LEASEBACK TRANSACTIONS UNDER § 162 (a)(3), INTERNAL REVENUE CODE [26 U.S.C. § 162(a)(3)].

Section 162(a)(3), Internal Revenue Code [26 U.S.C. § 162(a)(3)] provides that:

> "There shall be allowed as a deduction all the ordinary and necessary expenses paid or incurred during the taxable year in carrying on any trade or business, including —
>
> . . . .

> "(3) rentals or other payments required to be made as a condition to the continued use or possession, for purposes of the trade or business, of property to which the taxpayer has not taken or is not taking title or in which he has no equity."

In its opinion in the present cases, the Fourth Circuit held that a gift of property to a trust and its subsequent leaseback must be viewed as part of an overall transaction and stated that:

> "Real business purpose, therefore, must be shown to the transaction *as a whole* before any expenditures incident to elements of the transaction can be held as 'ordinary and necessary' business expenses deductible under § 162." Emphasis in Original. (Appendix 17a)

This application by the Fourth Circuit of the business purpose test to the gift as well as to the leaseback contravenes the decisions of all other Courts of Appeal that have decided the issue; and, in fact, the Fourth Circuit specifically rejected the rule laid down by the Seventh Circuit in *Skemp v. Commissioner*, 168 F. 2d 598 (7th Cir. 1948), and the Third Circuit in *Brown v. Commissioner*, 180 F. 2d 926 (3rd Cir. 1950), *cert. denied*, 340 U.S. 814 (1950).[1]

[1] See Appendix, infra, pages 16a and 18a. On page 16a the Fourth Circuit said: "We do not find *Skemp* compelling because the result in that case rests largely on a bifurcation of the overall transaction, an approach contrary to the holdings in this circuit." On page 18a it said: "*Brown* followed the bifurcated basis of decision in *Skemp* about which we have already expressed our disapproval." In this connection, the Fourth Circuit's statement, on page 18a of the Appendix, that "we do not think that our reasoning in the instant case is inconsistent with *Skemp*," was not intended to indicate a lack of conflict in the law applied by the two Courts of Appeal; instead, the Fourth Circuit was merely indicating that employing its theory of integration instead of the *Skemp* theory of bifurcation it could have reached the same *result* as the Seventh Circuit in *Skemp* if the *Skemp* facts had been before it.

The Seventh Circuit in *Skemp v. Commissioner*, 168 F. 2d 598 (7th Cir. 1948), treated the creation of the trust and leaseback separately; and the Court stated:

> "While the taxpayer voluntarily created the situation which required the payments of rent, the fact remains that the situation created did require the payments." Id. 600.

See also *Ingle Coal Corporation v. Commissioner*, 174 F. 2d 569 (7th Cir. 1949), for a reiteration of this rule by the Seventh Circuit.

The Third Circuit, in *Brown v. Commissioner*, 180 F. 2d 926 (3rd Cir. 1950), *cert. denied*, 340 U.S. 814 (1950), likewise treated the creation of the trust and leaseback separately; and the Court stated:

> "There is no suggestion that the two trusts in question were not created in good faith nor that they were not valid and irrevocable. By the trust agreements the taxpayers irrevocably conveyed to an independent trustee title to the land upon which the siding was located and the coal land. The trustee then leased them back to the taxpayers upon what were found by the Tax Court to be reasonable rents and royalties. It is true that this was done pursuant to a prior understanding between the taxpayers and the prospective trustee but we do not regard this point as significant. What is controlling is that there came into the picture a new independent owner, the trustee, who was in a position to and did require the payment of the rents and royalties as a condition to the continued use and possession of the lands by the taxpayers for the purposes of their business, and wholly without regard to whether their operations resulted in taxable income." Id. 929.

In *Brooke v. United States*, 468 F. 2d 1155 (9th Cir. 1972), the Court considered and rejected the "lack of busi-

ness purpose" argument asserted by the government and stated that:

> "Neither substance nor impact denies this transfer professional or economic reality." Id. 1158.

Thus, from the foregoing it is apparent that the action taken by the Fourth Circuit in the present cases is, by its own admission, in direct conflict with the Third, Seventh, and Ninth Circuits. Further, despite what the Fourth Circuit claims the Fifth Circuit says, the Fifth Circuit has never rendered an opinion on the question of whether a gift of property and its subsequent leaseback should be viewed as part of an overall transaction for purposes of determining whether there was a business purpose.[2] Of the Fifth Circuit cases involving situations of this sort, that Court has disposed of the question in the following ways:

In *Van Zandt v. Commissioner*, 341 F. 2d 440 (5th Cir. 1965), *cert. denied*, 382 U.S. 814 (1965), the Court stated:

> "[T]he ' . . . principal question is whether' the sale and leaseback ' . . . should be disregarded as a subterfuge for income tax purposes.' 188 F. 2d 531, 532. In answering that question, the Court then proceeded to tick off a number of factors which proved conclusively that there was no good business purpose for the transaction.

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[2] However, in a Tax Court case, dealing with a gift-leaseback situation, which the Fifth Circuit affirmed *per curiam*, the Tax Court stated:

> "The presence or absence of business purpose in lessor-lessee transactions of the type involved herein is not in and of itself determinative. The fact that there may be a business purpose for a transaction does not necessarily mean that the transaction has economic substance for tax purposes. Similarly, the lack of a business purpose does not necessarily mean that there is no such economic substance. Compare *Van Zandt* with *Alden B. Oakes.*" *Irvine K. Furman*, 45 T.C. 360, at 366, n. 9 (1966).

> "Whether viewed as a single or a multi-step transaction, the same is true here." Id. 443.

In other words, in *Van Zandt* the Court based its decision on a number of factors which, when applied to the facts in that case, resulted in a sham transaction, not on whether the transfers of the property involved should be treated as a single or multi-step transaction.

In *Audano v. United States*, 428 F. 2d 251 (5th Cir. 1970), the Fifth Circuit again based its decision on the fact that "the trusts established by taxpayer are a nullity for tax purposes." Id. 257. Likewise, in *W. H. Armston Co. v. Commissioner*, 188 F. 2d 531 (5th Cir. 1951), the Fifth Circuit stated:

> "We are of the opinion the Tax Court correctly held that the purported sale and lease arrangement between W. H. Armston Co., Inc., and its majority stockholder, Catherine Armston, was without substance and effect for tax purposes." Id. at 533.

Again the decision was based on the transaction as a whole being a sham, rather than requiring a business purpose for the initial sale. See also Tax Court cases which were affirmed *per curiam* by the Fifth Circuit: *Jack Wiles*, 59 T.C. 289 (1972), *aff'd* 491 F. 2d 1406 (5th Cir. 1974); *Irvine K. Furman*, 45 T.C. 360 (1966), *aff'd* 381 F. 2d 22 (5th Cir. 1967).

In *Mathews v. Commissioner*, ___ F. 2d ___, 36 AFTR 2d 75-___ (5th Cir. 1975), decided on October 1, 1975, the Fifth Circuit stated:

> " . . . it is not sufficient merely to serve up some 'business purpose' as some of the cases put it. The fact taxpayers can conjure up some reason why a businessman would enter into this sort of arrangement—tax consequences aside—does not foreclose inquiry. Rather, there must be 'economic reality.' "

And, in speaking of the gift and leaseback arrangement before it in *Mathews*, the Fifth Circuit stated:

> "Deduction of rental payments to such 'economic nullities' is not contemplated by § 162(a)(3)." Id. at ---.

Thus, once again, the Fifth Circuit has relied upon the "economic reality" of the transaction, and has not required that the initial step—the gift—be motivated by a business purpose.

It is submitted that the consistency of the other circuits is well founded, inasmuch as the rule followed by them was set forth by the Supreme Court in *Helvering v. Clifford*, 309 U.S. 331, 60 S.Ct. 554, 84 L.Ed. 788 (1940). There the Court stated:

> "Technical considerations, niceties of the law of trusts or conveyances, or the legal paraphernalia which inventive genius may construct as a refuge from surtaxes should not obscure the basic issue. That issue is whether the grantor *after the trust has been established* may still be treated * * * as the owner of the corpus." (Emphasis added.) 309 U.S. at 334, 60 S.Ct. at 556, 84 L.Ed. at ---.

[Although *Clifford* dealt with the question of whether the grantor of a trust might be taxed upon the trust's income, the principles enumerated therein are equally applicable, and have been applied by other courts, in determining whether a donor has retained such dominion and control over his gift to a family trust as to prevent him from deducting rents paid to such trust for his use of the donated property. *White v. Fitzpatrick*, 193 F. 2d 398, 401 (2nd Cir. 1951), *cert. denied*, 343 U.S. 928 (1952).]

The decision of the Fourth Circuit involved here is also in direct conflict with the longstanding rule of the Tax Court that in situations of the sort presented in the present cases

it is not necessary to inquire as to whether there was a business reason for making the gift but that the test of business necessity should be made by viewing the situation as it exists after the gift is made. *Jack Wiles*, 59 T.C. 289 (1974), *aff'd per curiam*, 491 F. 2d 1406 (5th Cir. 1974); *C. James Mathews*, 61 T.C. 12 (1973), *rev'd* __ F. 2d __, 36 AFTR 2d 75- ___ (5th Cir. 1975); *Sidney W. Penn*, 51 T.C. 140 (1968); *Alden B. Oakes*, 44 T.C. 524 (1965); *Albert T. Felix*, 21 T.C. 794 (1954).

Moreover, the decision of the Fourth Circuit in the present cases conflicts with decisions of the Third, Seventh, and Ninth Circuits not only in its requirement that the gift of property and its subsequent leaseback be integrated for purposes of applying the business purpose test, but also in its treatment of the significance of a trustee independent of the grantor. The significance of an independent trustee was clearly pointed out by the Court in *Brooke v. United States*, 468 F. 2d 1155, at 1157 (9th Cir. 1972), where it said that the decisions in *Brown v. Commissioner*, 180 F.2d 926 (3rd Cir. 1950), *Skemp v. Commissioner*, 168 F. 2d 598 (7th Cir. 1948), and *Van Zandt v. Commissioner*, 341 F. 2d 440 (5th Cir. 1965), "pivot on the issue of the independence of the trustee."[3]

These conflicts justify the grant of certiorari to review the judgment below. Rule 19.1(b), Rules of the Supreme Court of the United States.

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[3] The Fifth Circuit, prior to its decision in *Mathews v. Commissioner*, ____ F. 2d ____, 36 AFTR 2d 75- ____ (5th Cir. 1975), treated the independence of the trustee as being of great significance; however, in *Mathews*, the Fifth Circuit retreated to the position taken by the Fourth Circuit in the present cases. Therefore, the conflict in circuits as to the significance of the trustee's independence would now appear to have the Third, Seventh and Ninth Circuits on one side and the Fourth and Fifth Circuits on the other.

II. THE DECISION OF THE COURT BELOW RAISES SIGNIFICANT AND RECURRING PROBLEMS CONCERNING THE ADMINISTRATION AND INTERPRETATION OF THE FEDERAL INCOME TAX LAWS.

The Fourth Circuit, in the present cases, decided an important question concerning the administration and interpretation of the federal income tax laws and created confusion and a conflict of circuits relative thereto.

The widespread use of gift and leaseback arrangements throughout the United States and the position taken by the Internal Revenue Service as to the deductibility of rental payments in gift-leaseback situations gives great importance to the question decided by the Fourth Circuit and warrants its consideration by this Court.

The position of the Internal Revenue Service is well established by the fact that it has included in its list of "prime issues" the question of whether a taxpayer is entitled to deduct rental payments made to the trustees of a valid "Clifford Trust" when the payments are made for the use of property which the taxpayer had previously conveyed to the trustee and then leased back. Internal Revenue Manual, MT 1277-8, November 19, 1974.

"Prime issues" are those which, as a matter of policy, the Internal Revenue Service will not concede or compromise. Therefore, it is apparent that the question of the deductibility of rental payments in gift-leaseback arrangements will, because of the position of the Internal Revenue Service, result in recurring litigation until this Court provides appropriate guidelines.

Moreover, the Fourth Circuit has added confusion to the question by its decision in the present cases. Before this decision the Courts had followed the general rule that in

determining whether or not to allow deductions for rents paid as the result of disposition-leaseback transactions the issue was determined by the *bona fides* of it. The rule was most clearly stated in *Brooke v. United States*, 468 F. 2d 1155 (9th Cir. 1972), as follows:

> "The fundamental issue presented involves the sufficiency of the property interest transferred. The transfer of a sufficient property interest justifies the taxation of the donees and deduction of the rental payments under 26 U.S.C. § 162(a)(3) as ordinary and necessary business expenses by the donor." Id. 1157.

All cases involving disposition-leaseback situations, prior to the present case, were determined on that basis; and, if a sufficient property interest was transferred, the donee was taxed and the donor-lessee was allowed a deduction regardless of the purpose of the transfer, while if a sufficient property interest was not transferred the opposite result ensued.[4]

The Fourth Circuit by its opinion in the present cases has superimposed the additional requirement that the transfer must be for a business purpose. Such a requirement is not demanded by the law and results in the creation of great uncertainty and doubt in the disposition-leaseback area. Moreover, the rule announced by the Fourth Circuit has the effect of condemning outright and absolutely the deductibility of

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[4] The recently decided case of *Mathews v. Commissioner*, ___ F. 2d ___, 36 AFTR 2d 75-___ (5th Cir. 1975), apparently creates an exception to the consistent approach discussed in the text. In that case, the Fifth Circuit elected to treat the legal entity created by the establishment of a valid trust as a mere "flyspeck of legal title under state law . . . " Id. at ___. The Petitioners submit that the Fifth Circuit's disregard of a valid trust with a trustee independent of the settlor serves only to further confuse the entire area and strengthen the need for a review thereof by this Court.

ordinary and necessary business expenses incident to *all* gift and leaseback arrangements, a result not contemplated even by the Fifth Circuit in *Van Zandt v. Commissioner*, 341 F. 2d 440 (5th Cir. 1965), *cert. denied*, 382 U.S. 814 (1965), the case most heavily relied upon by both the government and the Fourth Circuit in the present cases. As pointed out by the United States Tax Court in *Alden B. Oakes*, 44 T.C. 524 (1965):

> " . . . *it is not necessary for us to inquire as to whether there was a business reason for making the gift. Admittedly there was none.* . . . As the Court of Appeals emphasized in *Van Zandt*, what is good business purpose 'ultimately depends on the factual evaluation of the particular case.' The facts in this case favor petitioners." Id. at 532.

Furthermore, it is an elementary and fundamental principle of federal tax law that a gift "proceeds from a 'detached and disinterested generosity,' . . . 'out of affection, respect, admiration, charity or like impulses," and not from a business motive or purpose. *Commissioner v. Duberstein*, 363 U.S. 278, 285, 80A S.Ct. 1190, 1197, 4 L.Ed. 2d 1218, ___ (1960). Thus, it is apparent that the Fourth Circuit's decision in the present cases will result in the disallowance of ordinary and necessary business expenses incident to all gift and leaseback arrangements.

The need for clarification of issues of importance in the administration of the income tax laws, particularly where a conflict between Courts of Appeal exists, constitutes a valid basis for certiorari. *Commissioner v. Duberstein*, 363 U.S. 283, 80A S.Ct. 1190, 4 L. Ed. 2d 1218 (1960). Therefore, for the foregoing reasons and because both lower courts and potential litigants urgently need the assistance and direction of this Court in a proper determination of this issue, the Petitioner's request for certiorari should be granted.

III. IN DETERMINING THAT THE TRUSTEE IN THE PRESENT CASES WAS NOT INDEPENDENT OF THE PETITIONERS, THE FOURTH CIRCUIT VIOLATED THE REQUIREMENT OF RULE 52(a) OF THE FEDERAL RULES OF CIVIL PROCEDURE [FED. R. CIV. P. RULE 52(a), 28 U.S.C.] THAT FINDINGS OF FACT SHALL NOT BE SET ASIDE UNLESS CLEARLY ERRONEOUS.

Rule 52(a), Fed. R. Civ. P., 28 U.S.C., provides that "Findings of fact shall not be set aside unless clearly erroneous. . . . " The independence of a trustee in a gift and leaseback arrangement is a question of fact. *C. James Mathews*, 61 T.C. 12, at 14 and 19 (1973), *rev'd* ___ F. 2d ___, 36 AFTR 2d 75- ___ (5th Cir. 1975); *Robert F. Zumstein*, ¶ 73,045 P-H Memo T.C. (1973). See also *Southeastern Canteen Co. v. Commissioner*, 410 F. 2d 615, at 619 (6th Cir. 1969). Furthermore, the question of whether a sale-and-leaseback is *bona fide* has been treated by the government and the Fourth Circuit as a question of fact. *American Realty Trust v. United States*, 498 F. 2d 1194 (4th Cir. 1974). See also, *Hutton v. United States*, 501 F. 2d 1055 (6th Cir. 1974), which held that whether a transaction is a "sham" for tax purposes is a finding of fact subject to Rule 52(a). In addition, this Court has held that the question of whether there has been a gift, for income tax purposes, is a question of fact, and not a question of law. *Commissioner v. Duberstein*, 363 U.S. 278, 80A S.Ct. 1190, 4 L.Ed. 2d 1218 (1960). See also *Altman v. Commissioner*, 475 F. 2d 876 (2nd Cir. 1973); *Harper v. United States*, 454 F. 2d 222 (9th Cir. 1971).

The "clearly erroneous" rule applies to appeals by the government as well as those by other litigants. *United States v. Yellow Cab Co.*, 338 U.S. 338, 70 S.Ct. 177, ___ L. Ed. ___ (1949). Furthermore, the rule applies even when documentary evidence comprises most or all of the proof or

when the case is decided on undisputed facts, as in the present cases. *Commissioner v. Duberstein*, 363 U.S. 278, 80A S.Ct. 1190, 4 L.Ed. 2d 1218 (1960) (findings based on undisputed facts); *Nalle v. First National Bank of Baltimore*, 412 F. 2d 881 (4th Cir. 1969) (documentary evidence comprised much of the proof); *Bowman v. Curt G. Joa, Inc.*, 361 F. 2d 706 (4th Cir. 1966) (District Court findings based on affidavits and briefs); *Summers v. Watkins Motor Lines*, 323 F. 2d 120 (4th Cir. 1963) (findings based on transcript); *Custom Paper Products Co. v. Atlantic Paper Box Co.*, 469 F. 2d 178 (1st Cir. 1972) (findings based solely on documentary evidence); *H. K. Porter Company, Inc. v. Goodyear Tire & Rubber Company*, 437 F. 2d 244 (6th Cir. 1971) (findings based solely on documentary evidence); *Worthen Bank & Trust Company v. The Franklin Life Insurance Company*, 370 F. 2d 97 (8th Cir. 1966) (findings based on pleadings, exhibits, answers to interrogatories and affidavits, both parties having moved for summary judgment); *Transducer Patent Company v. The Renegotiation Board*, 492 F. 2d 247 (9th Cir. 1975) (findings based on evidence "largely documentary"); *Lundgren v. Freeman*, 307 F. 2d 104 (9th Cir. 1962) (findings based on documentary evidence).

In the present cases, the District Court found that "the independence of the corporate trustee is about as firmly established as one could imagine." Appendix 8a. Therefore, the Fourth Circuit, in its consideration of the cases on appeal, was bound by Rule 52(a) to respect the District Court's finding that the corporate trustee was independent unless such finding was "clearly erroneous." *American Realty Trust v. United States*, 498 F. 2d 1194 (4th Cir. 1974); *Bowman v. Curt G. Joa*, Inc., 361 F. 2d 706 (4th Cir. 1966); *Summers v. Watkins Motor Lines*, 323 F. 2d 120 (4th Cir. 1963). Notwithstanding the requirements of Rule 52(a), however, the Fourth Circuit made its own findings that the independence of the corporate trustee in the present cases

was "largely illusory." (Appendix 16a). The rationale for this finding was as follows:

> "The bank had virtually no function save to hold legal title and to receive and remit the rental payments arranged by the settlors at the time the trusts were created. The terms and conditions of the leases were fixed before the trusts were created and the durations of the leases were identical to those of the trusts. There was literally no area in which the broad powers of management vested in the bank as trustee could operate." Appendix 16a.

The Petitioners submit that the District Court's findings as to the independence of the trustee were amply supported by the evidence in the cases, and were therefore not "clearly erroneous." On the other hand, the conclusion of the Fourth Circuit is based on no evidence at all, but rather solely on speculation as to how the corporate trustee would react to a breach of the lease agreement by the Petitioners. The Petitioners submit that the action of the Fourth Circuit is patently erroneous. As the District Court stated:

> "It may be true, as the government seems to argue, that in reality the trustee here is going to respect the wishes of the taxpayers, but the legal effect of the transaction into which they have entered must be judged by the instruments as executed and not on speculation." Appendix 8a.

See also *Skemp v. Commissioner,* 168 F. 2d. 598, 599 (7th Cir. 1948).

The Petitioners respectfully submit that the Fourth Circuit, by reversing the District Court's findings as to the trustee's independence and thereby violating the requirements of Rule 52(a), has rendered a decision which "has so far departed from the accepted and usual course of judicial proceedings . . .

as to call for an exercise of this court's power of supervision." Rule 19.1(b), Rules of the Supreme Court of the United States. The Petitioners further submit that this Court, in the exercise of its responsibility for the proper functioning of the federal judiciary, should grant the writ of certiorari in the present cases in order to ensure that the function of District Courts in passing on disputed questions of fact is respected.

CONCLUSION

For the foregoing reasons, this Petition for Writ of Certiorari should be granted.

Respectfully submitted,

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